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APPENDIX A

Statutes Involved

Federal Aviation Act

Sec. 1002. [*72 Stat. 788, 49 U.S.C. 1482*]

* * *

Power to Prescribe Rates and Practices
of Air Carriers

(d) Whenever, after notice and hearing, upon complaint, or upon its own initiative, the Board shall be of the opinion that any individual or joint rate, fare, or charge demanded, charged, collected or received by any air carrier for interstate or overseas air transportation, or any classification, rule, regulation, or practice affecting such rate, fare, or charge, or the value of the service thereunder, is or will be unjust or unreasonable, or unjustly discriminatory, or unduly preferential, or unduly prejudicial, the Board shall determine and prescribe the lawful rate, fare, or charge (or the maximum or minimum, or the maximum and minimum thereof) thereafter to be demanded, charged, collected, or received, or the lawful classification, rule, regulation, or practice thereafter to be made effective: *Provided,* That as to rates, fares, and charges for overseas air transportation, the Board shall determine and prescribe only a just and reasonable maximum or minimum, or maximum and minimum rate, fare, or charge.

* * *

Suspension of Rates

(g) Whenever any air carrier shall file with the Board a tariff stating a new individual or joint (between air

carriers) rate, fare, or charge for interstate or overseas air transportation or any classification, rule, regulation, or practice affecting such rate, fare, or charge, or the value of the service thereunder, the Board is empowered, upon complaint or upon its own initiative, at once, and, if it so orders, without answer or other formal pleading by the air carrier, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, fare, or charge, or such classification, rule, regulation, or practice; and pending such hearing and the decision thereon, the Board, by filing with such tariff, and delivering to the air carrier affected thereby, a statement in writing of its reasons for such suspension, may suspend the operation of such tariff and defer the use of such rate, fare, or charge, or such classification, rule, regulation, or practice, for a period of ninety days, and, if the proceeding has not been concluded and a final order made within such period, the Board may, from time to time, extend the period of suspension, but not for a longer period in the aggregate than one hundred and eighty days beyond the time when such tariff would otherwise go into effect; and, after hearing, whether completed before or after the rate, fare, charge, classification, rule, regulation, or practice goes into effect, the Board may make such order with reference thereto as would be proper in a proceeding instituted after such rate, fare, charge, classification, rule, regulation, or practice had become effective. If the proceeding has not been concluded and an order made within the period of suspension, the proposed rate, fare, charge, classification, rule, regulation, or practice shall go into effect at the end of such period: *Provided,* That this subsection shall not apply to any initial tariff filed by any air carrier.

Sec. 1006. [*72 Stat. 795, as amended by 74 Stat. 255, 75 Stat. 497, 49 U.S.C. 1486*]

Orders Subject to Review; Petition for Review

(a) Any order, affirmative or negative, issued by the Board or Administrator under this Chapter, except any order in respect of any foreign air carrier subject to the approval of the President as provided in section 801 of this Chapter, shall be subject to review by the courts of appeals of the United States or the United States Court of Appeals for the District of Columbia upon petition, filed within sixty days after the entry of such order, by any person disclosing a substantial interest in such order. After the expiration of said sixty days a petition may be filed only by leave of court upon a showing of reasonable grounds for failure to file the petition theretofore.

* * * *

Review by Supreme Court

(f) The judgment and decree of the court affirming, modifying, or setting aside any such order of the Board or Administrator shall be subject only to review by the Supreme Court of the United States upon certification or certiorari as provided in section 1254 of title 28, United States Code.

Administrative Procedure Act [*Chapter 5 of Title 5, U.S.C.*]

§ 553. Rule making

(a) This section applies, according to the provisions thereof, except to the extent that there is involved—

(1) a military or foreign affairs function of the United States; or

(2) a matter relating to agency management or personnel or to public property, loans, grants, benefits, or contracts.

(b) General notice of proposed rule making shall be published in the Federal Register, unless persons subject thereto are named and either personally served or otherwise have actual notice thereof in accordance with law. The notice shall include—

(1) a statement of the time, place, and nature of public rule making proceedings;

(2) reference to the legal authority under which the rule is proposed; and

(3) either the terms or substance of the proposed rule or a description of the subjects and issues involved.

Except when notice or hearing is required by statute, this subsection does not apply—

(A) to interpretative rules, general statements of policy, or rules of agency organization, procedure, or practice; or

(B) when the agency for good cause finds (and incorporates the finding and a brief statement of reasons therefor in the rules issued) that notice and public procedure thereon are impracticable, unnecessary, or contrary to the public interest.

(c) After notice required by this section, the agency shall give interested persons an opportunity to participate in the rule making through submission of written data,

views, or arguments with or without opportunity for oral presentation. After consideration of the relevant matter presented, the agency shall incorporate in the rules adopted a concise general statement of their basis and purpose. When rules are required by statute to be made on the record after opportunity for an agency hearing, sections 556 and 557 of this title apply instead of this subsection.

(d) The required publication or service of a substantive rule shall be made not less than 30 days before its effective date, except—

(1) a substantive rule which grants or recognizes an exemption or relieves a restriction;

(2) interpretative rules and statements of policy; or

(3) as otherwise provided by the agency for good cause found and published with the rule.

(e) Each agency shall give an interested person the right to petition for the issuance, amendment, or repeal of a rule.

* * *

APPENDIX B

UNITED STATES COURT OF APPEALS

FOR THE DISTRICT OF COLUMBIA CIRCUIT

[No Opinion]

No. 75-2020—September Term, 1976

AMERICAN AIRLINES, INC., DELTA AIR LINES, INC., EASTERN AIRLINES, INC., and TRANS WORLD AIRLINES, INC.,

Petitioners,

v.

CIVIL AERONAUTICS BOARD,

Respondent,

THE NATIONAL PASSENGER TRAFFIC ASSOC., INC.,

Intervenor.

On Petition for Review of Orders of the Civil Aeronautics Board.

Before:

WRIGHT and ROBB, Circuit Judges, and GESELL,* District Judge.

JUDGMENT

This cause came on to be heard on a petition for review of orders of the Civil Aeronautics Board and was argued

* Of the United States District Court for the District of Columbia, sitting by designation pursuant to 28 U.S.C. § 292(a) (1970).

by counsel. While the issues presented occasion no need for an opinion, they have been accorded full consideration by the court. *See* Local Rule 13(c).

Our consideration of this case convinces us that it does not come within the principle announced in *Moss* v. *CAB*, 430 F.2d 891 (D.C. Cir. 1970). We are further of the view that the case is moot since the suspended tariffs have been withdrawn by the airlines.

On consideration of the foregoing, it is ORDERED and ADJUDGED by this court that the petition for review of the Board's orders is hereby dismissed.

Per Curiam

For the Court:

/s/ GEORGE A. FISHER
GEORGE A. FISHER
CLERK

FILED DEC 17 1976
GEORGE A. FISHER
CLERK

Appendix B

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 75-2020—September Term, 1976

AMERICAN AIRLINES, INC., DELTA AIR LINES, INC.,
EASTERN AIRLINES, INC., and TRANS WORLD AIRLINES, INC.,
Petitioners,

v.

CIVIL AERONAUTICS BOARD,
Respondent,

THE NATIONAL PASSENGER TRAFFIC ASSOC., INC.,
Intervenor.

Before:

WRIGHT AND ROBB, Circuit Judges;
GESELL,* United States District Judge for the United States District Court for the District of Columbia

ORDER

On consideration of the petition for rehearing filed by petitioners, it is

ORDERED by the Court that petitioners' aforesaid petition is denied.

Per Curiam
For the Court:
/s/ GEORGE A. FISHER
GEORGE A. FISHER
Clerk

FILED FEB 3 1977
GEORGE A. FISHER
CLERK

* Sitting by designation pursuant to 28 U.S.C. § 292(a).

Appendix B

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 75-2020—September Term, 1976

AMERICAN AIRLINES, INC., DELTA AIR LINES, INC.,
EASTERN AIRLINES, INC., and TRANS WORLD AIRLINES, INC.,
Petitioners,

v.

CIVIL AERONAUTICS BOARD,
Respondent,

THE NATIONAL PASSENGER TRAFFIC ASSOC., INC.,
Intervenor.

Before:

BAZELON, Chief Judge;
WRIGHT, MCGOWAN, TAMM, LEVENTHAL, ROBINSON, MACKINNON, ROBB AND WILKEY Circuit Judges

ORDER

The suggestion for rehearing *en banc* filed by petitioners having been transmitted to the full Court, and no Judge having requested a vote with respect thereto, it is

ORDERED by the Court, *en banc,* that petitioners' aforesaid suggestion for rehearing *en banc* is denied.

Per Curiam
For the Court:
/s/ GEORGE A. FISHER
GEORGE A. FISHER
Clerk

FILED FEB 3 1977
GEORGE A. FISHER
CLERK

APPENDIX C

Order 75-6-72

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D.C.

Adopted by the Civil Aeronautics Board
at its office in Washington, D.C.
on the 13th day of June, 1975

Docket 27947

Domestic passenger fare increases proposed by

VARIOUS CARRIERS

Docket 27417

Petition by the

DEPARTMENT OF TRANSPORTATION

requesting the Board to issue a show cause order with respect to the standard load factor

---

ORDER OF INVESTIGATION AND SUSPENSION

By tariff revisions marked to become effective on various dates from June 15 through July 1, 1975,[1] all domestic trunkline and regional carriers operating within the 48 contiguous states and the District of Columbia propose to

[1] Revisions to Airline Tariff Publishers Company, Inc., Agent C.A.B. Nos. 229, 246, and 249.

extend the four percent fare increase which become effective on November 15, 1974 beyond its expiration date of June 30, 1975. Some carriers propose to limit the extension to an additional six and one-half months and have included a new expiration date of January 14, 1976, while others contend that it should be made a permanent part of the fare structure. In addition, five carriers propose a further increase in fares of either five or six percent. A summary of the carriers' proposals appears in Attachment A.

All carriers argue that both fuel and non-fuel costs have continued to rise, and that a roll-back in fares by four percent would be financially unsound in light of the very poor financial results in the first quarter of 1975. Five carriers contend that costs (primarily fuel cost) have risen to such an extent that they are not being offset by the higher fares previously permitted and that a further increase is now mandatory. No carrier contends that a further increase would be inconsistent with the Board's standards adopted in the *Domestic Passenger-Fare Investigation* (DPFI). However, several express concern over the possible adverse effect of an additional increase at this time, essentially because of the "unsettled" state of the economy.

The complainants, on the other hand, argue that continuing the four percent increase, and in particular implementing a further increase, will only cause a further decline in airline financial results because higher fares will cause greater numbers of passengers to foresake air travel. The complainants allege that the root cause of the carriers' financial difficulty is their inability or unwillingness to match capacity to traffic, and that the recent increases in fares have created a growing disincentive to fly.

A summary of the carriers' justifications appears in Attachment B. Complaints have been filed by the Council

on Wage and Price Stability (Council) against TWA and American; against TWA, American and Eastern by the Board's Office of the Consumer Adovocate (OCA); and against several carriers by the National Passenger Traffic Association, Inc. (NPTA). A summary of these complaints and answers thereto appears in Attachment C.

In addition, the Department of Transportation (DOT) has petitioned the Board for an order to show cause why ratemaking load-factor standards should not be increased, particularly in the longer-haul trunkline markets. A summary of DOT's petition and answers thereto appears in Attachment D.

THE FARE PROPOSALS

The carriers have purported to follow all the *DPFI* standards in evaluating the industry's present revenue need, and most of those which are proposing an additional increase beyond the four percent have gone the further step of making the full discount-fare adjustment.[2] All carriers use calendar 1974 as the base period. Although the computations vary somewhat from carrier to carrier, they are as a general rule substantially similar, and support the carriers' claims that their proposed fares do not exceed those allowable under the Board's *DPFI* standards as so far applied. Most have computed the unadjusted or actual 48-state rate of return on investment (ROI) at approximately 8 percent, and typically at approximately 10 percent as adjusted for Phase 5 discount fares, standard seating, and the load factor standard. Without the full discount-fare adjustment the carriers generally estimate

[2] In evaluating previous fare-increase proposals the Board has adjusted ROI only for those discount fares specifically investigated in the *DPFI* (youth, family and Discover America).

that an approximate 12 percent fare increase is needed to raise the industry ROI to 12 percent. With the fare increases of 5 or 6 percent, including the full discount-fare adjustment, the carriers estimate an ROI of between 10.38 and 11.5 percent (Eastern does not compute the final adjusted ROI, but estimates that an 8 percent fare increase would be required to reach the 12 percent ROI standard).

The Board's analysis of present revenue need produces a different result. In making our analysis, we have refined the cost-escalation factor, and have made an adjustment for aircraft utilization for the first time. We have also made the full discount-fare adjustment, as have some carriers. Finally, we have used a different base period, since the tariff-filing lead time did not permit the carriers to use the most recent data for the year ended March 31, 1975, as we have done.

The ROI computed on this basis, including annualization of the four percent fare increase, is 11.29 percent, four points above the actual ROI of 7.28 percent realized by the trunkline industry. (See Attachment E.) Nevertheless, it remains below the 12 percent return which the Board has found reasonable for ratemaking purposes and, accordingly, retention of the four percent is warranted on a temporary basis at this time. However, we are not now persuaded that the carriers should be permitted to incorporate the November 15, 1974 four percent fare increase as a permanent part of the fare level. The economic situation is uncertain, as is the impact of the various major discount-fare programs which the carriers have established in recent months. For these reasons, we will suspend the proposals which would extend the four percent increase indefinitely. Our analysis also indicates that the proposed increases over and above the present fare level would result

in an excessive ROI for the industry, and should be suspended.

As indicated, our ROI computations reflect various modifications in the approach we have followed in evaluating previous fare-increase proposals. It should be stressed that none of the foregoing modifications reflect a departure from the basic principles of the *DPFI*. The full discount-fare adjustment is merely an implementation of a policy enunciated in our 1972 decision in Phase 5 of the *DPFI* and thus has been long heralded. The adjustment for aircraft utilization is required in order to avoid reflecting in the future-period fare level the abnormally low utilization experienced in 1974 as a result of fuel constraints which have been subsequently relieved. The modification in the inflation factor merely reflects the fact that fuel costs are no longer rising as rapidly as they did in the base period. We have also refined the belly-cargo revenue-offset adjustment to reflect annualization of cargo-rate increases as a necessary corollary to the annualization of fare and cost increases. These various adjustments and other considerations underlying our conclusions are discussed in detail below.

The cost-escalation factor is intended to adjust base period costs to reflect the level of costs experienced at the effective date of the fare increase. The factor previously used, and used here by the carriers in their justifications, was based on the increase in operating expense per available-seat-mile (at the standard load factor) from one year to the next. This technique accomplishes the desired result as long as unit costs are increasing at a reasonably steady rate. However, this does not appear to be the situation at this time and, as a consequence, we have developed a refined methodology for developing the escalation factor

insofar as it is influenced by fuel prices. While we have continued to use the traditional approach with respect to non-fuel costs, we have estimated the price of fuel as of July 1, 1975 to be 1.5 cents a gallon higher than the average for the first quarter 1975. This basically reflects the impact of the $1.00-a-barrel tax increase on imported crude oil which was effected in February 1975. The impact of that increase, estimated to be about 1.3 cents a gallon for aviation fuel, is expected to flow through to the airlines sometime around the middle of the second quarter. Our total computed cost factor is 7.85 percent, about one half that computed by most carriers. Some of this difference, however, stems from the fact that we are using a more recent base period which reflects higher cost levels than the data used by the carriers.

We have made a ultilization adjustment in evaluating these proposals because the higher load factors which approached the ratemaking standard during 1974 resulted from reduced frequencies and aircraft utilization, rather than from traffic growth as had been contemplated in the *DPFI*. The present methodology makes no adjustment to account for higher load factors due solely to less efficient utilization of aircraft (zero utilization when an aircraft is grounded). However, this element has not previously been of material consequence. We believe such an adjustment in the present atypical circumstances is wholly consistent with the fundamental principle which evolved from the *DPFI*, that the general fare level should not be burdened by unnecessary capacity. Accordingly, we have adjusted 1974 utilization rates, by carrier and by aircraft type, to reflect their 1972 experience.[3] For the year ended

[3] This is the most recent normal calendar-year prior to the development of the fuel crisis in 1973. We have made no adjustment in the case of those carriers whose 1974 utilization exceeded that in 1972.

March 1975, the overall adjusted increase in utilization equated to a $33,996,000 decrease in depreciation and insurance cost, and a $285,266,000 decrease in investment and interest expense. We believe this approach provides a reasonable adjustment in present circumstances.[4]

As indicated, we have concluded that it is now appropriate to make the full discount-fare adjustment. The carriers have been on notice for over two years that the Board would eventually make such an adjustment. Nevertheless, in recent months they have established a number of major discount fares in an effort to stimulate traffic growth which has sagged because of the downturn in the economy, and to fill the substantial number of additional seats they have placed in service. We recognize that the general economic downturn and consequent decline in domestic passenger growth may well warrant discount-fare experimentation. However, it does not follow that the fundamental Phase 5 principle that full-fare traffic not be burdened by non-cost-based discount fares should be ignored. To the contrary, if anything, these circumstances would seem to require that the Board now take the necessary steps to avoid burdening the regular fare level.[5] This modification raises the ROI by about 2.5 points.

In summary, after making the adjustments described above, the industry's ROI remains under the 12 percent standard. While as discussed in detail later, we believe

[4] We have incorporated into the utilization adjustment four grounded B-747's of Continental representing $66 million of investment.

[5] In most of the Board's recent orders involving major discount-fare proposals the carriers have been forewarned that the fares would be subjected to the Phase 5 adjustment. A notice of proposed rulemaking dealing with the details of the adjustment methodology will be issued shortly.

that a review of the load-factor standard is now indicated, an adjustment for present purposes would not be warranted. In these circumstances, a rollback of the four percent increase permitted last November does not appear warranted.

At the time the four percent fare increase was introduced last November, the Board members were divided as to whether it was justified. Since that time, however, the carriers' unit costs have continued to escalate at a rapid rate. Thus, their unit costs (after various *DPFI* adjustments) for the year ended June 30, 1974—the base year employed in the Board's earlier assessment of this fare increase—averaged 3.54 cents per available seat-mile (¢/ASM). Using what it deemed a reasonably representative cost-escalation factor, the Board projected a 1974 year-end unit-cost level of 3.93 ¢/ASM, and the dissenting members argued for a somewhat lower figure. However, the carriers' subsequently reported operating results for the year ended March 31, 1975—the base period being employed here—show a *DPFI*-adjusted unit-cost level of 3.98 ¢/ASM. Application of the refined cost-escalation factor and other adjustments described above points to a 1975 midyear unit-cost level of 4.23 ¢/ASM, which is nearly eight percent higher than the 1974 year-end level projected last fall. This substantial rise in the unit-cost level compels the conclusion, even by those who argued that the fare increase was unjustified at the time it was introduced, that it cannot now be rolled back but must be permitted to remain in effect until January 14, 1976.

In our judgment, the complainants do not indicate error in the foregoing analysis.[6] The complaints of the Council

[6] In addition to its allegations which are basically similar to those of the other complainants, NPTA once again alleges that

and OCA center on the possible adverse impact on traffic.[7] The Council contends that fares should be rolled back to the level prevailing prior to the 4 percent increase last November—and perhaps to an even lower level—unless the Board can satisfy itself, among other things, that the present price elasticity of airline traffic will in fact insure that higher fares will produce higher total revenues. However, the Council provides no evidence to support the proposition that traffic is now so elastic that continuing the four percent increase will have a negative impact on revenues. On the other hand, a number of factors suggest that this is not the case. For example, yield was up 14.7 percent in the year ended March 1975 over the previous year, yet traffic remained relatively constant (down —.46 percent and revenues rose by 14.2 percent. During the early

the carriers should not be permitted fare increases because they have failed to take advantage of a cost-sharing proposal of NPTA. That proposal would in effect compensate NPTA members for the ticketing and reservation services they provide for company employees, which according to NPTA would be considerably less than the present 7 percent commission which the airlines pay commercial travel agencies. NPTA claims that this costs the airlines about $100 million a year. The Board has in the past declined to consider the merits of NPTA's proposal in connection with pending fare increases, and NPTA has provided no reason which persuades us that we should now reverse that policy. The merits of OCA's allegations as to TWA's relative efficiency aside, continuation of present fare levels would be warranted even were TWA's results eliminated from *DPFI* adjusted totals.

[7] Numerous references are made to the increases in domestic air fares over the past year and a half, the cumulative effect of which is undeniably substantial. However, reciting fare increases without providing any comparative basis is meaningless. For example, comparing 1974 over 1972 (just prior to the round of increases repeatedly referred to), the increase in yield expressed in constant dollars is only 2.3 percent, which cannot be considered unreasonable in light of the substantially greater impact petroleum price increases have had on the airline industry versus the economy in general.

months of 1974, when the then recent cancellation of a number of discount fares resulted in rather substantial increases in yield (on top of the six percent fuel-related increase which was permitted in mid-April 1974), traffic did not drop as dramatically as would be expected in an elastic market. Rather, during the peak summer months of June through September, a considerable amount of discount fare traffic shifted to full fares. This consumer reaction does not suggest a substantially elastic market.[8] Moreover, we cannot ignore the fact that the airline industry is in unanimous agreement that continuation of the four percent is necessary.

The complainants also contend that the carriers should not expect to earn a 12 percent ROI in the present economic climate. A basic concept of the *DPFI* is that in periods of low load factor the carriers' actual ROI will tend to be below the 12 percent ratemaking standard and, conversely, will exceed the standard when load factor rises above 55 percent.[9] Thus, for ratemaking purposes, the Board does not recognize a decline in load factor caused by economic recession or any other factor. The Board's policy is, therefore, consistent with the complainants' contention that carriers should not expect a 12 percent return in the present circumstances. The adjusted ROI approaches the recognized level only because of the severity of the Board's ratemaking adjustments. The actual ROI

[8] Along similar lines, the Council and OCA express concern for the discretionary traveler, contending that the solution to recent traffic declines is to reduce the cost of air travel so as to generate new business. However, this argument ignores the influx of many greatly reduced promotional fares initiated by the carriers in recent months; such as 7-30 day excursion fares in all markets over 750 miles, night coach excursion fares, "no frill" fares in certain markets, and other more selectively available fares.

[9] See Order 71-4-59, April 9, 1971, Opinion, pages 72-74.

for the year ended March 31, 1975 was only 7.28 percent, and without the four percent increase now marked to expire this could drop significantly. As long as actual load factors remains low, whether because of the economic climate or for whatever reason, the airline industry's actual earnings will be below the recognized ROI. This is not inconsistent with the fluctuation in earnings of other industries. In summary, the complainants' concern about permitting the industry to earn a 12 percent ROI in the present economic climate stems from a lack of understanding of the Board's policy.[10]

In the area of cost control, the complainants' primary concern, with the exception of NPTA, appears to be with alleged deficiencies evidenced by the declining load factor, particularly insofar as it is caused by the addition of capacity. However, under the standard load factor methodology, the decline in load factor is not reflected in the carriers' claims, or in the Board's calculation of revenue need.

The Load-Factor Standard

Without offering any factual support or legal basis for doing so, the complainants urge the Board to apply a higher load-factor standard in evaluating the instant proposals. A partial answer to this contention is that implementation of the full discount-fare adjustment in effect implies a significantly higher load factor than 55 percent. Since all discount fares are eliminated in our evaluation,[11]

[10] It is important to distinguish between ratemaking ROI and actual ROI, with the stringent adjustment we have made, the former is about 11 percent. However, the actual ROI is only 7.28 percent.

[11] Children's fares are not excluded since they are regarded as part of the basic fare structure.

the load-factor standard becomes a full-fare standard, and the industry's fare level is thus tied to the revenues generated by full-fare revenue passenger-miles. However, since actual yield is less than the full-fare yield used for ratemaking purposes, the industry would need to realize a load factor substantially in excess of 55 percent in order to achieve the recognized ROI.[12]

Moreover, at this point, it is impossible to predict the consequences of raising the full-fare load-factor standard to 60 or 65 percent as the complaints suggest. Since these represent system-average load factors, it is possible that operations at this level would create serious adequacy-of-service problems. In addition, since load factors are now trending downward, it would be inconsistent with past Board policy to reverse the trend abruptly for ratemaking purposes, and would place the carriers in an untenable earnings position. We refer here to the Board's decision to phase in the present 55 percent standard partly because the economic climate prevailing at that time was inhibiting traffic growth, and therefore the carriers' ability to bring capacity into line with demand.

Nevertheless, we are persuaded that circumstances have changed sufficiently in the years intervening since our Phase 6B *DPFI* decision to warrant a reevaluation of the 55 percent load-factor standard, as requested by DOT. DOT contends that raising the standard to at least 65 percent, particularly in longer-haul markets, would result in lower coach fares for all passengers in return for somewhat less convenient service, and would be consistent with

[12] Indeed, achievement of a 12 percent ROI in 1974 would have required an actual load factor somewhat above 60 percent when the discount-fare traffic is taken into account.

the national need for fuel efficiency.[13] However, we do not believe that a show cause order would provide an effective forum.

The level of the standard load factor is of major consequence to the public, since it represents that level of service which the public is asked to pay for and which over the longer term can expect to receive. It also has a major impact on carrier earnings when actual load factors deviate substantially from the standard, and thus discourages inefficient scheduling practices. For example, the base period used in evaluating the December 1, 1973 five percent fare increase was the year ended June 30, 1973. At that time, the carriers' load factor was 52.1 percent (48.2 after adjusting for standard seating) and, as a result, in excess of $500 million in operating expense was disallowed.[14] Subsequent to the Board's decision on this standard,[15] the carriers' load factors gradually rose toward the 55 percent, as expected. Nevertheless, until the impact of the fuel crisis on scheduling practices, the actual 48-state load factors remained considerably below the standard. As load factors increased due to fuel-related schedule reductions, the impact of the load-factor adjustment diminished sharply. For the year ended June 1974, the base period used in evaluating the November 1974 four percent fare increase, the load factor was 55.2 percent (53.1 with standard seats), and the load-factor adjustment disallowed $145 million in operating expense.

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[13] Several carriers—Allegheny, Braniff, Continental, Eastern, Frontier, National, Southern, United and Western—filed comments along with the Aviation Consumer Action Project. A summary of these comments, DOT's petition and answer appear in Attachment D.

[14] This reflects elimination of only the Phase 5 discount fares.

[15] Phase 6B of the *DPFI*.

DOT cites the fact that the *DPFI* findings on load factor were based upon 1967-1969 experience. Now, just six years later, the unprecedented rise in fuel prices is having a significant impact on costs and most probably will cause significant changes in the carriers' scheduling practices as they seek to control consumption. We agree with DOT that the present standard needs to be reevaluated in order to insure that such an important ratemaking input reflects what all sources indicate will be the continuing impact of fuel on the economics of the airline industry. No details need be cited to prove the major change that has taken place over the last year as a direct result of the fuel crisis What concerns us most is the indefinite duration of that change, and the apparent lack of any real possibility that the situation will revert to the years of low fuel prices and unlimited supplies. Indeed, current national policy indicates that prices can only rise in the future as we seek fuel independence. Tentative estimates are that the Administration's present fuel policy could ultimately raise the domestic airlines' fuel bill between $640 million and $1.5 billion annually.[16]

The fundamental question which is presented in this situation is whether or not the cost/quality of service relationship inherent in the present load-factor standard has been sufficiently increased on the cost side to warrant some balancing modification on the quality of service side. In other words, largely because of fuel price increases, the cost of operating aircraft has risen more rapidly than costs generally. In terms of real dollars, it costs more today than in previous years to provide the same level of service. In terms of constant dollars, the current cost level is 9.8

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[16] At present, $2 of the contemplated $3-per-bbl. increase in the tariff on imported crude has been imposed.

percent above 1972. The load-factor standard would need to be raised to 60.4 percent if this cost increase were to be absorbed through a decrease in the quality of service rather than passed on to the passenger. While future increases in fares may prove to be warranted, current conditions nevertheless dictate a reexamination of the basic cost/quality of service relationship as reflected in the load-factor standard so that at least some portion of the escalating cost level may be offset by an adjustment in the quality of service. Also, we have previously indicated our intentions of focusing upon the desirability of applying the standard load-factor adjustment by class of service (Order 74-12-109, December 27, 1974, footnote 59). Accordingly, our reexamination of the load-factor standard will encompass this issue as well.

We have concluded to undertake a rulemaking proceeding, rather than pursue the show-cause procedure urged by DOT, as the most effective means of dealing promptly with the question of the load-factor standard. A formal public hearing would be extremely time consuming, and we believe these issues need to be explored as expeditiously as possible. On the other hand, the rulemaking approach should provide an adequate forum in which all parties can fully present their views.[17]

The Board is also considering a reexamination of issues relating to the rate of return. On the one hand, substantial questions have been raised in recent months in the public arena as to the reasonableness of the 12 percent standard. On the other hand, there have been changes in the capital market since the Board's decision on this issue in the *DPFI*. Under these circumstances, the time may be ripe for a review of this issue.

[17] DOT's petition in Docket 27417 will be consolidated into the rulemaking proceeding.

We view the periodic reevaluation of previously established ratemaking principles and standards in the light of possibly altered conditions as an appropriate exercise of our responsibilities. However, the institution of a proceeding in which the Board examines these principles and standards should not be construed as any prejudgment or commitment to change.

Accordingly, upon consideration of the tariff filings, the justifications, complaints, answers, and all relevant matters, the Board concludes that the proposals to increase domestic fares beyond current levels, and those proposals which would continue the present fare level indefinitely, may be unjust, unreasonable, unjustly discriminatory, unduly preferential, unduly prejudicial, or otherwise unlawful and should be investigated. We further conclude that the fares should be suspended pending investigation. We find that the complaints do not set forth sufficient facts to warrant investigation of the proposals which would continue the present level of fares until January 14, 1976, and the requests therefor and consequently the requests for suspension will be denied, and the complaints dismissed.

Accordingly, pursuant to the Federal Aviation Act of 1958, and particularly sections 204, 403, 404, and 1002 thereof,

It Is Ordered That:

1. An investigation be instituted to determine whether the provisions described in Attachment F hereto, and rules, regulations and practices affecting such provisions, are or will be unjust, unreasonable, unjustly discriminatory, unduly preferential, unduly prejudicial, or otherwise unlaw-

ful, and, if found to be unlawful, to determine and prescribe the lawful provisions and rules, regulations, or practices affecting such provisions;

2. Pending hearing and decision by the Board, the provisions described in Attachment F hereto are suspended and their use deferred to and including September 12, 1975, unless otherwise ordered by the Board, and that no changes be made therein during the period of suspension except by order or special permission of the Board;

3. Except to the extent granted herein, the complaints in Dockets 27862, 27864, 27886, and 27887 are hereby dismissed;

4. The investigation ordered herein be assigned before an Administrative Law Judge at a time and place hereafter to be designated;

5. A copy of this order be filed with the aforesaid tariffs and be served on the domestic scheduled certificated air carriers, the Allied Pilots Association, the Civil Aeronautics Board's Office of Consumer Advocate, the Council on Wage and Price Stability, the Department of Transportation, and the National Passenger Traffic Association, which are hereby made parties to this proceeding, and upon the Aviation Consumer Action Project.

This order will be published in the Federal Register.

By the Civil Aeronautics Board:

Edwin Z. Holland
Secretary

(SEAL)

Timm, Member, Filed the Attached Concurring Statement.

Timm, Member, Concurring Statement:

When the Board instituted the *Domestic Passenger-Fare Investigation,* it did so out of a desire to introduce the elements of stability and predictability into what had theretofore been a variable and unreliable area of *ad hoc* decision-making. It alarms me to see those principles and the results already achieved by their implementation in the present coherent and orderly fare regime jeopardized by the new era of unpredictability which the Board seems to herald in this decision.

Several new adjustments which the Board has made in computing the air transportation industry's revenue need are of particular concern since they impose novel and unannounced standards upon which the industry and the public have not been given the opportunity for comment.

The new utilization factor, for example, arbitrarily adjusts 1974 utilization to the 1972 carrier experience. This simplistic and somewhat broad-brush approach should have been announced by the Board well in advance of this decision so that the public and the industry could have submitted comments and replies to the proposal. An ROI computation excluding this utilization adjustment would produce a 10.53 percent instead of an 11.29 percent ROI. The end result would be that a further 1.5 percent fare increase above the present level including the 4 percent increase of last year would still not bring the industry-wide ROI to 12 percent. I believe that such an adjustment is inevitable and desirable but I believe that fairness and administrative due process require advance notice.

The full discount-fare adjustment which the Board is implementing here is also a matter of concern to me, since it prejudges the rule-making procedure which would be the more appropriate means of arriving at this adjustment.

Furthermore it chooses to deal with military traffic in the same way as other discount passengers, in effect considering them full-fare-paying passengers and subjecting them to the Phase 5 adjustment. I trust that this approach means that the Board will not discourage carrier discontinuance of these military fares since it would be unconscionable to require their continuation in a fare regime while simultaneously penalizing the carriers and their shareholders for offering them.

As to the rule-making proceeding which the Board is initiating today to reexamine the load factor standard, I believe that this vital question which will have such far-reaching effects on the public interest in general and on air transportation economics in particular should be fully explored in a formal public hearing in which all parties may fully participate. The halfway measure which the Board offers here as a compromise with DOT's show-cause technique will sacrifice thoroughness for speed and will impede a full exploration of all points of view. I believe a similar approach should be taken in any reexamination of the level and application of ROI.

However, it seems to me that all of these policy changes, which may result in sharp deviations from past Board actions and orders, should not be dealt with precipitously but should be thoroughly examined in an orderly manner by the Board. I do not believe that the instant question before us today provides an appropriate vehicle for a re-assessment of Board policy relative to specific formulae or petitions presently being considered by the Board. The only procedure consonant with the Board's statutory obligations is for the Board to communicate its proposed policy change to the staff and the public who may then study and comment on these principles prior to their implementation

by the Board. Without this procedure, any standard set by the Board at any time may, under the pressure of time deadlines, cease to be a standard, and become merely a brief benchmark that will lead to short-term, case-by-case, *ad hoc* decision-making. The result will be a bewildered public, bewildered industry and financial communities, and a bewildered Board, all wondering whether our U.S. transport system can endure beyond the transitory moment.

In conclusion, I concur in the ultimate result which the Board has reached today, but I do so without prejudice to future fare filings that may reflect the upward march of costs. I note that, despite the application of almost every conceivable downward adjustment of carrier revenue need, which I discussed above, the Board has found today that the economic circumstances in the air transportation industry fully justify last year's 4 percent fare increase at the present time and in effect entitle the carriers to an increase of about 1 percent over their present fares.

/s/ Robert D. Timm

ATTACHMENT A

SUMMARY OF PROPOSALS

	Continuation of the 4 percent	Continuation of the 4 percent plus an additional 5 percent	Continuation of the 4 percent plus an additional 6 percent
American	X[1]		X[1]
Braniff	X		
Continental	X		
Delta	X		
Eastern	X		X[1]
National	X		
Northwest	X		
TWA	X	X[1]	
United	X[1]	X[1]	
Western	X		
Airwest	X		
Allegheny	X[1]		
Frontier	X[1]	X[1]	
North Central	X[1]		
Ozark	X		
Piedmont	X[1]		
Southern	X		
Texas International	X		

[1] Marked to expire with January 14, 1976.

ATTACHMENT B

Summary of Carrier Justifications

In support, the carriers allege, *inter alia,* that the decline in the economy has placed the industry in a severe revenue deficiency which will remain as long as these economic conditions continue; that a reduction in the general fare level, in the middle of the summer peak travel season, would seriously exacerbate the financial difficulties facing the industry; that fares must be set in recognition of the continuing cost increases being experienced by the industry and that it is obvious from the most recent financial results, that fare increases have not been forthcoming in time to offset cost increases; and, that if the four percent fare increase were allowed to expire, the industry return could very well fall to a negative return and thus the continuation of present fares cannot be economically disputed.

American, Eastern, TWA, and United propose to increase fares five to six percent over present levels. In support of their proposals, these carriers allege, *inter alia,* that cost increases, particularly aviation fuel, have far outgained revenues, and that even with the *DPFI* ratemaking standard adjustments the requested increases are fully justified. Further, these carriers contend that even after the modifications and changes suggested by Members Minetti and West in the Board methodology of evaluating industry rate of return, the requested increases will fall short of the Board's return standard, and without the increase will approximate only seven percent. They emphasize that these *pro forma* regulatory returns are not real-world achievable returns, and as a practical matter cannot be achieved without outside forces such as the mandatory fuel allocation program which was largely re-

sponsible for the reasonable earnings of some carriers in 1974. The carriers contend that they cannot, nor should they be expected to stop the inflation process, and while they are making every effort to curtail costs, the current and projected increases in aviation fuel are beyond the control of the airline industry. They note that since November 1974, when the Board granted the carriers a four percent increase, the average price per gallon of fuel has risen almost 16 percent for the domestic trunk industry.

Those carriers urging continuation of the present level of passenger fares state that there is no question that after application of *DPFI* standards a further increase is warranted, but because of the uncertain effect such an increase could have on recovery, both on the general economy and air transportation in particular, they feel that fares should not be increased further at this time. There is a general agreement that because of the present and potential fuel price situation, an increase in fares may be unavoidable in the near future. They further assert that a rollback in the present level of fares would only create very significant losses, since it is unlikely that such a small fare decrease would have any stimulative effect.

ATTACHMENT C

Summary of Complaints and Answers

Council on Wage and Price Stability (Council)

The Council has filed a complaint against the proposals of both TWA and American seeking suspension and investigation of both the renewal of the 4 percent increase and the further increases. The Council states that its interest in filing the complaint is "to see that in reaching its

decisions, the Board also takes into account the potential inflationary and anti-competitive consequences of its actions, and acts to minimize those consequences." The Council believes that fares should be rolled back to the level prevailing before the 4 percent increase unless the Board can satisfy itself that: (1) the present price elasticity of air passenger traffic is such that higher air fares will in fact produce higher total revenues; (2) the carriers have made every effort to reduce their operating expenses—that fares should only be increased if required to meet uncontrollable increases in costs; and (3) no fare increase should be granted under present circumstance for the purposes of raising the carriers' return on investment to the 12 percent level. In the view of the Council, the justifications filed by American and TWA fail to establish grounds for fare relief in each of these areas. Finally, the Council asserts that these are not normal times and the carriers have no right to expect to earn "normal", *i.e.*, 12 percent, rates of return during the current period of high inflation and severe recession.

Office of the Consumer Advocate (OCA)

The OCA has filed complaints against the retention of the 4 percent increase and the additional 5 percent increase proposed by TWA and 6 percent proposed by American and Eastern. The OCA asserts that the airline industry is rapidly pricing itself out of the market and that it is, therefore, "incumbent upon the Board to step in and prevent TWA, and other carriers considering fare increases from self-destruction." Otherwise, states the OCA, air travelers will be limited to business travelers and those individuals in the higher income brackets who can afford the luxury of air travel. The OCA contends that higher

load factors are imperative and that the public must not be required to pay for high costs attributable to the present situation of overcapacity.

With respect to TWA in particular, OCA contends that that carrier's poor performance is not representative of or comparable to the industry's efficiency and accordingly should not be the basis of an industry-wide rate increase. OCA asserts that the load factor situation is one cause of American's high first quarter 1975 loss and that the answer to spiraling costs is not adding more capacity as American has done but reducing capacity unilaterally. In reviewing efficiency measurements, OCA notes that Eastern's productivity—*i.e.* revenue ton miles generated per employee is 25 percent less than that for the entire industry. Finally, OCA alleges that the carriers have not adequately reduced controllable costs, and that there exists a price increase/traffic decrease spiral which must be stopped.

National Passenger Traffic Association (NPTA)

The NPTA is a nationwide association representing over 300 companies and business organizations which operate business travel departments providing airline ticketing and reservation services for company employees. The complainant requests that the Board deny both the renewal of the 4 percent increase and any further increase by any carrier. The NPTA asserts that a fare increase would seriously reduce traffic and thus be counter-productive. The NPTA further contends that the carriers have not demonstrated that they are taking all reasonable steps to control their non-fuel related costs. In particular, the complainant cites the failure of the carriers to agree to a cost sharing with the NPTA which allegedly has resulted in a greater use of commercial travel agents by business travelers and thus higher costs to the carriers.

Answers of the Carriers[1]

TWA argues that the complaints by OCA and the Council fail to discuss the proposed fare increase within the context of the *DPFI* and that the complainants would have the Board adopt an ephemeral emotional standard which would be contrary to the Board's legal power. The carrier asserts that it sufficiently justified both the extension of the existing 4 percent and proposed 5 percent fare increases using industry-wide data and the *DPFI* methodology, and that OCA's contention that TWA's performance should not be the basis of an industry-wide rate increase is not relevant. The carrier further asserts that the ratemaking ROI would be only 11.19 percent even if TWA were eliminated from the industry totals. TWA claims that while the proposed 5 percent and retention of the 4 percent fare increase would yield an 11.19 percent regulatory ROI, the real world ROI would be —0.47 percent due to the vicissitudes of the economy and the 55 percent load factor standard which the carrier feels is unattainable in the present economic climate. TWA charges that the Council's complaint attacks the *DPFI* and avoids the issue of whether or not the proposed fares are justified according to present legal standards. The carrier asserts that the

[1] The Department of Transportation (DOT) filed an answer to the Council's complaint stating that it "reluctantly" supports both retention of the 4 percent increase and further 5 and 6 percent increases. In addition, the answer reiterates DOT's support of a 65 percent ratemaking load-factor standard, and asserts that the 12 percent ROI should be a long-range goal rather than an inflexible yardstick for all fare increase requests. Also, the Allied Pilots Association has filed a statement in support of American's proposed increase. APA states that the central problem facing the carriers is the mounting fuel prices and that there is no reason why the airline industry alone should be called upon to swallow such cost burdens.

airline industry has made significant efforts to retain traffic and generate new traffic as evidenced by the extensive promotional fare programs of recent months.

In response to OCA's allegations that TWA has failed to exercise capacity restraint, the carrier asserts that probably no other carrier in the industry has made more stringent efforts to hold down capacity in relation to the soft traffic experienced this year than has TWA. Over the past winter TWA grounded six wide body aircraft and in the forthcoming months it will have four L-1011 aircraft grounded in the early part of the summer and six grounded by August. TWA contends that the fact that its drastic actions in curtailing capacity have not solved its problems is reflective of the fact that unilateral capacity reductions cannot spare a carrier the difficulties of a declining market. Finally, TWA asserts that contrary to the view of OCA, its non-fuel costs are not out of line with other carriers, but its fuel costs are, and this is a matter over which it has no control.

American, Eastern, and United answer, *inter alia,* that the complaints are actually petitions for reconsideration of *DPFI* standards and as such are not germane to the instant case. The carriers state that the industry ROI will remain below 12 percent even with the requested increase, particularly since sharply higher fuel costs seem inevitable with President Ford's recent energy message and assertions by Arab leaders that oil prices will soon rise. The carriers argue that the *DPFI* methodology prohibits inefficient carriers from being rewarded unwarranted fare increases. Application of these *DPFI* standards results in the elimination of more than one billion in industry operating and interest expense, and $626 million in industry investment. In addition, the carriers contend that compari-

sons of the airline industry to non-regulated businesses are inherently unfair since the latter have broad discretion in reducing losses while the air carriers have public responsibilities which preclude such unilateral acts.

The respondents argue that this is not a case of expecting "normal" profits but simply a case that they must have revenue increases in order to overcome their present position of no profits.[3] They contend that the carriers have not achieved the Board's rate of return standard for many years and that in competing with other industries for capital, the airline industry is at or near the bottom in any measure of American business.

Finally, the carriers allege that the complainants' contentions that the 4 percent increase of last fall resulted in the traffic downturn during the first quarter of 1975 are unsubstantiated. Among other factors, they cite the fact that first quarter 1974 traffic results were distorted by the fuel crisis, and that adjusting for this fact, traffic declined only 1.4 percent in the first quarter of 1975. Moreover, it is alleged that even with the 4 percent increase last fall, fares for much of the travelling public have actually declined by reason of the Board's Phase 9 (Fare Structure) decision and the introduction of various discount fares so that average passenger-mile yield has *decreased* 4.4 percent.

ATTACHMENT D

DOT's Petition

On January 17th, 1975, the United States Department of Transportation (DOT) filed a petition with the Board stating that the Board should take immediate steps to direct

[3] American claims that with a fare rollback, adjusted regulatory rate of return for the industry would be less than the interest paid on the carriers' debt.

the carriers to show cause why ratemaking load factor standards should not be increased. In support of its petition DOT states its belief that the excursion fares recently approved for the airlines[1] should be approved for only a short period of time pending consideration of an increase in ratemaking load factors to 60-65 percent. DOT believes the excursion fare to be discriminatory since it would be limited to selected travelers and estimates that "if implemented on an industry-wide basis, would reduce the fare level by about 4 percent."

DOT contends that the increase in ratemaking load factors to 60-65 percent, at cost levels then prevailing, would result in a fare reduction for all coach passengers of approximately 10 percent. Such action, DOT asserts, would promote expanded air travel, encourage the carriers to operate at higher load factors, and increase fuel efficiency. DOT believes that raising the load factor standard to at least 65 percent, particularly in the longer haul markets,[2] would result in lower coach fares for all passengers in return for somewhat less convenient service and would be consistent with the national need for fuel efficiency.

DOT states that the proposed changes must take place in the competitive environment versus the two alternatives—capacity agreements or a government controlled fuel allocation program. Both alternatives, DOT believes, may result in the passenger receiving service at higher load factors than those the passengers pay for and would receive in a competitive environment. Finally DOT asserts that even if recovery of fuel cost increases through increased fares is necessary at some future time, the public will have

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[1] Order 75-1-72, January 17, 1975 wherein the Board approved "Bicentennial" excursion fares in markets over 1,500 miles.

[2] DOT states that, to provide reasonably convenient service, raising short-haul ratemaking load factors may not be appropriate.

the benefits of increased fuel efficiency stemming from higher load factors and the fares will still be below the level which would have been necessary if the Board had continued to utilize present load factor levels in ratemaking.

In response to comments, DOT states that the data base for the load factor portion of the *DPFI* was 1967, 1968, and 1969 experience and the final decision was rendered in April 1971. Were it not for significantly changed conditions, DOT states that it would not recommend a change in the load factor standard it recommended over four years ago; but two key changes have occurred which warrant reexamination of the 1971 load factor standard. First, the increased cost of imported crude oil has caused the Administration to embark on a program of reducing fuel use. And second, the increased cost of fuel has resulted in substantial fare increases.

DOT further states that it does not believe that the 65 percent standard is appropriate for all markets, but that there are many markets in which higher load factors are acceptable and warranted, and that such higher load factors could provide significant benefits to the public in terms of more reasonable rates. Concerning the alternative posed by American Airlines to allocate fuel, DOT answers that such action does not benefit passengers in that passengers are entitled to receive service in a competitive environment at the level implied in those rates and that the allocation program might well result in many passengers paying for one level of service and receiving a lower level of service (*i.e.*, higher load factors and greater delay). Concerning another alternative, promotional fares, DOT asserts that unless properly structured, such fares debase the fare structure and burden other fare passengers; thus they do not achieve the basic objective DOT seeks.

Summary of Comments

Allegheny

Allegheny contends that DOT's pleading is imprecise as to its objective and devoid of factual or analytical support for the propositions advanced. The carrier asserts that the use of a show cause procedure to accomplish DOT's objectives is contrary to the established ratemaking scheme of the Act which empowers the Board to prescribe changes in fares only after notice and hearing.

Aviation Consumer Action Project (ACAP)

ACAP supports the reduction in the general domestic passenger fare level proposed by DOT and requests that the Board conduct an investigation and hearing to determine the proper amount of such reduction. ACAP contends that the carriers appear to recognize, in the form of various discount fare requests, that the cost of air travel now exceeds the ability to pay of a large number of potential passengers. ACAP agrees with DOT that fare decreases should take the form of an across-the-board reduction in coach fares, rather than the complex discount plan, but alleges that DOT has not presented adequate financial data to determine the proper amount of such a decrease. Finally, ACAP asserts it (sic) belief that the Board cannot properly set fare levels through a show cause order, but only after notice and hearing.

Braniff

Braniff asserts that the DOT petition rests on the unsupported assumption that fares could be reduced if the Board adopted a 65 percent load factor, wholly ignoring the tremendous increases in fuel costs being concurrently advo-

cated by the very Administration of which DOT is a part. The carrier contends that the request for an order to show cause is in material respects a petition for reconsideration of Order 71-4-54, by which load factor standards were first established, and of Order 74-3-81, March 18, 1974, wherein trunkline standards were affirmed, but standards for the shorter haul local service carriers were rescinded. In summary, Braniff alleges that the DOT petition has no factual predicate and that it simply rehashes arguments recently made and rejected in the barely concluded (except for remand) *DPFI*.

Continental

Continental opposes the petition of DOT for three reasons. First, the petition is vague in that it offers no parameters for defining "longer haul markets," nor does it provide any explanation or justification for choosing 65 percent. Second, the Board has already dealt specifically with DOT's request in Phase 9. And third, Continental is concerned that the use of an *average* 65 percent load factor standard will cause significant public inconvenience by virtue of the fact that, to attain this average, the carriers necessarily will have to operate many flights fully booked at great inconvenience to passengers.

Eastern

Eastern states that DOT has provided nothing to demonstrate the actual financial effect upon the trunk carriers. It contends that the traffic increase needed just to break-even with DOT's 10 percent fare cut is 15.9 percent and DOT has made no showing that this traffic increase could ever be achieved or even accommodated on existing ca-

pacity, or that the resulting load factor would be "reasonably attainable."

Frontier

Frontier asserts that DOT has completely ignored the fact that even under current fare levels the industry has not come close to achieving the 12 percent rate of return prescribed by the Board. Rather, the carrier contends, DOT has blandly assumed a 10 percent reduction in fares will miraculously generate enough new traffic to offset lost revenues, as well as justifying new ratemaking load factors of 60 to 65 percent. Frontier submits that regardless of the pressures in favor of lowering the cost of air transportation and saving fuel, the Board cannot abdicate its responsibility to foster "sound economic conditions," and should not abandon the principles of the *DPFI* when DOT has not submitted a shred of evidence or economic support to demonstrate that the years of hearings and analysis upon which the DPFI is founded are unreliable.

National

National alleges that the Board has already dealt with a similar proposal by DOT in Order 74-3-82, March 18, 1974, concluding that the massive record of the *DPFI* is insufficient to reach any firm conclusions as to the validity of the DOT proposal on passenger service quality; and that it would be entirely improper to use a show cause procedure at this point to attempt to implement the plan. In a sense, contends National, DOT is advocating ratemaking by the Board without a hearing which would violate Section 1002 of the Act and/or the decision of the court in *Moss vs. C.A.B.*, USCA (D. C. Circuit). No. 23,627, denied July 9, 1970.

Southern

In the case of the local service carriers such as itself, Southern contends that DOT's vision of the economics passed through to the public in the form of higher load factors and lower fares is simply unattainable. The carrier agrees with DOT that if the arguments have any validity at all, such validity is solely and exclusively confined to the longest haul "trunkline" markets.

United

United's principal objection to the DOT petition is its attempt to avoid proper ratemaking procedure through an improper use of the show cause procedure. United states that as the Board explicitly stated in Order 73-2-30, the show cause procedure is not appropriate in cases which "raise controversial and complex questions of fact, law or policy" and in which the relief requested will have more than "a minimal impact on competing certificated carriers," and clearly, the facts are in controversy. United further contends that DOT offers no support for its proposed change in a standard only established after an extensive evidentiary hearing in the *DPFI* that considered the complicated and controversial issues involved; and that the impact of the DOT proposal on the industry is more than "minimal."

Western

Western endorses the position that the petition for an order to show cause is contrary to Section 1002(d) of the Act. The carrier contends that DOT has failed to establish that an average load factor of 65 percent is attainable in long-haul markets given the present state of the econ-

omy and the airline industry, or that such a high average load factor would be desirable from the travelling public's point of view. Western alleges that, in effect, the request by DOT is an improperly filed petition for reconsideration of the Board's recently issued opinions on reconsideration concluding Phases 6B and 9 of the *DPFI*.

ATTACHMENT E

DOMESTIC TRUNK INDUSTRY RATE OF RETURN ON INVESTMENT 48-STATE SCHEDULED PASSENGER SERVICE

For the Twelve Months Ended
March 31, 1975
(dollar amounts in thousands)

	Actual	*DPFI Adjustments*[1]	*Other Adjustments*[2]
RPM's (Millions)	105,435	99,971	97,958
ASM's (Millions)	196,893	181,765	178,105
Load Factor	53.5%	55.0%	55.0%
Yield	7.7327¢	8.0575¢	8.2927¢
Passenger Revenue	$8,152,952	$8,055,180	$8,123,368
Operating Revenue	$8,361,926	$8,264,154	$8,332,342
Operating Expense	7,816,941	7,239,575	7,516,623
Operating Profit	$ 544,985	$1,024,579	$ 815,719
Interest	235,951	215,824	195,956
Income Before Tax	$ 309,034	$ 808,755	$ 619,763
Income Tax @ 48%	148,336	388,202	297,486
Net Income	$ 160,698	$ 420,553	$ 322,277
Return Element	$ 396,649	$ 636,377	$ 518,233
Investment	$5,446,233	$4,981,647	$4,590,873
R.O.I.	7.28%	12.77%	11.29%

[1] Removal of all discount fares; standard seating; and 55 percent standard load factor.

[2] Includes Column 2 adjustments plus cost factor, annualization of fare increases, plus adjustments for untilization, grounded aircraft, and belly cargo.

ATTACHMENT F

TARIFF C.A.B. No. 229 ISSUED BY AIRLINE TARIFF PUBLISHING COMPANY, AGENT

Supplement No. 3

Supplement Nos. 2, 4, 5 and 6 insofar as the supplements would cancel the four percent negative surcharge effective July 1, 1975 in Supplement No. 1.

TARIFF C.A.B. No. 246, ISSUED BY AIRLINE TARIFF PUBLISHING COMPANY, AGENT

Supplement No. 6 insofar as the supplement would cancel the four percent negative surcharge effective July 1, 1975 in Supplement No. 1 on behalf of carriers other than AL, AA, BN, FL, PI and UA.

TARIFF C.A.B. No. 249, ISSUED BY AIRLINE TARIFF PUBLISHING COMPANY, AGENT

Supplement Nos. 8, 10, 18, and 21.

Supplement Nos. 6, 9, 11, 14, 15, 17, and 20 insofar as the supplements would cancel the four percent negative surcharge effective July 1, 1975 in Supplement No. 1 on behalf of carriers other than AL, AA, FL, NC, PI and UA.

The suspension of the above supplements does not stay the cancellation of supplements other than Supplement No. 1.

Order 75-8-99

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Adopted by the Civil Aeronautics Board
at its office in Washington, D. C.
on the 19th day of August, 1975

Docket 27947

Domestic passenger-fare increases proposed by
VARIOUS CARRIERS

Docket 27417

Petition by the

DEPARTMENT OF TRANSPORTATION

requesting the Board to issue a show cause order with respect to the standard load factor

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ORDER DENYING PETITIONS FOR RECONSIDERATION

By Order 75-6-72, June 13, 1975, the Board permitted the carriers to extend the four percent fare increase which became effective on November 15, 1974 for a further period through January 14, 1976. At the same time, the Board suspended proposals of five carriers to increase fares above their current level.[1] Eastern, American, and TWA have

[1] American Airlines, Inc. (American) and Eastern Air Lines, Inc. (Eastern) proposed a six percent increase, while Trans World Airlines, Inc. (TWA), United Air Lines, Inc. (United), and Frontier Airlines, Inc. proposed a five percent increase.

now petitioned for reconsideration of that suspension, alleging that the Board erred in abandoning principles it has previously utilized in the evaluation of proposed general fare increases, and that it has "indiscriminately juggled figures in order to avoid the necessity for a fare increase." [2]

Specifically, petitioners contest the following adjustments made by the Board:

1) A full discount-fare adjustment rather than adjustment for only those discount fares considered in Phase 5 of the *Domestic Passenger-Fare Investigation, (DPFI);*

2) An aircraft utilization adjustment to reflect 1972 experience;

3) A modification in the methodology used to compute the cost inflation factor;

4) An annualization of cargo-rate increases in conjunction with the belly-cargo adjustment.

The petitioners contend that correction for alleged errors in the Board's computations leads to the unquestionable conclusion that a further increase in fares is necessary, and that the corrections are fully justified as proper under standards prescribed by the Board.[3]

[2] Both TWA and Eastern also address the Board's decision to undertake a rule-making proceeding to reexamine the present load-factor standard. Both carriers assert that the most effective and efficient procedure would be a formal evidentiary hearing, that the question of a proper load-factor standard involves complex and complicated issues that can only be resolved on the basis of a full and adequate formal record. The Board will dispose of the petitions insofar as they are directed to this question by subsequent order.

[3] Answers to the petitions were received from the National Passenger Traffic Association (NPTA) and National Airlines, Inc.

Upon review of the petitions and all other relevant matters, the Board finds that they do not establish error in its ultimate conclusion, nor do they otherwise provide information which would support lifting the Board's suspension.

The Board's current evaluation of fare proposals is rooted directly in its decisions in the *DPFI* and it has now been four years since the Board first implemented the ratemaking standards developed in that investigation.[4] During this period, the Board has dealt with several fare-increase proposals, and each time has incorporated further refinements in methodology in a continuing effort to implement more accurately the basic ratemaking principles in the context of the particular operational circumstances existing at the time the increase was requested.

The petitioners contend that the Board cannot legally make adjustments not previously made until the carriers have been given an opportunity to comment on their validity. In so doing, they appear to imply a deviation from the basic objectives toward which the ratemaking standards developed in the *DPFI* are directed. We perceive no inconsistency between adherence to those principles and change in analytical methodology. The refinements which

(National). NPTA asserts that in Order 75-6-72 the Board has not substantially deviated from the *DPFI* standards but, rather, has properly applied the principles as announced in the *DPFI* to the evolution of changing facts and circumstances within the industry. National's answer simply supports the point contained in the petitions of the other three carriers. United Air Lines, Inc. (United) filed a telegraphic answer in support of TWA's petition, stating that continued upward price pressures make the industry outlook even more pessimistic than when the five percent increases were filed.

[4] Orders 71-4-59/71-4-60, April 9, 1971, first applied the interim standard load factor of 52.5 percent.

we have made in methodology have been for the sole purpose of more effectively reflecting the ratemaking approach laid down in the *DPFI*. To freeze the methodology would be to inhibit the ability of the Board to perform its regulatory functions in the light of changing conditions and to make the most accurate possible assessment of future conditions. We do not agree that the Board is obligated to give the carriers "an opportunity to comment" on the validity of adjustments we deem necessary in a suspension case prior to investigation. If that were the case the Board's suspension powers would be seriously compromised. In any event, carriers have the right which they have here exercised to seek reconsideration of a suspension order.

In the past, the Board has incorporated an adjustment of base-period results to reflect annualization of fare increases which had taken place during the base year and has applied a cost inflation factor to reflect the level of costs which would prevail as of the effective date of the tariff. We note that the petitioners do not object to the Board's use of a cost inflation factor, *per se*, but rather contest the method of calculating that factor for present purposes of evaluation. It is our opinion that the further adjustments which we have made in this instance to which the petitioners object are reasonable in light of the abnormalities which occurred during the base period, and represent necessary modifications in methodology if the Board's basic ratemaking approach is to be preserved.

Discount-Fare Adjustment

As we indicated in our previous order, the carriers have been on notice for more than two years that the Board would in due course make the full discount-fare adjustment.

Indeed, the minority statement issued in connection with the initial 4 percent increase in November 1974 urged that it be made at that time, and several carriers have reflected the full adjustment in their justifications. The importance of moving to a full adjustment now is underscored by the marked reemphasis on discount fares in recent months and the prospect for its continuation.[5] Failure by the Board to take this step might serve to encourage the introduction of questionable fares and create a further long-term pressure on the general fare level. This decision is fully consonant, in our opinion, with the fundamental principle of the *DPFI*, that full-fare traffic not be burdened with the cost of carrying passengers not traveling on cost-based fares.

In making the full adjustment for discount-fare travel, the Board first determined the traffic carried during the base year from reports filed under Phase 5 of the *DPFI*.[6] The Board then calculated the number of passengers who would have needed to be generated for the fare to break even. The generated passengers were then deducted from actual traffic results and 100 percent of related traffic and capacity costs were eliminated, as well as a 100 percent disallowance of related interest and investment.

[5] In its recent orders disposing of these discount fares, the Board indicated its intention to treat the fares within the parameters of Phase 5; *i.e.*, that it would include traffic moving on the fares in the discount-fare adjustment in subsequent evaluations of proposed general fare increases. See for example: Orders 75-1-72; January 17, 1975; 75-1-131, January 30, 1975; 75-3-17, March 6, 1975; 75-3-102, March 27, 1975; and 75-4-47, April 9, 1975.

[6] As Eastern points out, approximately 50 percent of the traffic is in the "All other" category. This is due to the fact that Discover America, youth, and family fares no longer account for the major share of discount-fare traffic. Review of this category reveals that it does not contain a significant amount of non-discount fare traffic.

American contends that the 100 percent elimination of interest and investment related to discount-fare carriage is inconsistent with the 75 percent factor utilized by the Board in making other adjustments, notably the annualization of fare increases. It appears upon reexamination that the Board's analysis does contain an inconsistency. However, it lies not in the discount-fare adjustment as American contends, but in the adjustment to interest and investment related to annualization of past fare increases. The Board calculates the effect of a fare increase at —.7 elasticity and, accordingly, the number of passengers decreases. In the past, 100 percent of both capacity and traffic costs related to this decline in traffic has been deducted from carrier expenses. A corresponding full reduction should be made in related interest and investment, a correction which is reflected in Appendix A.

Military Fares

In Order 75-6-72, the Board eliminated traffic and costs related to all discount fares other than children's fares, which the Board has stated should be treated as part of the basic fare structure for purposes of assessing revenue need.[7] The petitioners argue that military fares should similarly be recognized and should not, therefore, have been included in the Board's adjustment for discount fares. American contends that, if military fares are to be treated like other discount fares, the carriers must also have the corresponding freedom which they now lack to cancel the fares if they deem it appropriate. Eastern asserts that the Board's inclusion of military fares runs counter to its conclusion in Phase 5 of the *DPFI* that such fares "are justified under the policy of Section 102(a) of the Act to

[7] Order 72-12-18, December 5, 1972, p. 75, fn. 91.

properly adapt the air transportation system to the needs of the national defense."[8] In the Board's opinion, resolution of this issue should appropriately await the rulemaking proceeding dealing with implementation of Phase 5. However, we have decided to exclude military fares from the discount-fare adjustment in the interim, the effect of which is incorporated into the calculations set forth in Appendix A.

Utilization Adjustment

The petitioners argue that the utilization adjustment applied by the Board was not developed in any phase of the *DPFI* and should not, therefore, be used by the Board until all parties have had an opportunity to present their views concerning its validity. Additionally, they contend that this adjustment duplicates the disallowance of capacity resulting from application of the load-factor standard; that a more proper comparison would be between the current utilization rate and a 1972 ratemaking utilization rate; that 1974 results reflect carrier adjustments to external events; and that the costs incurred should be fully recognized in the absence of any finding that actual utilization rates were the result of anything other than "honest economic, and efficient management."

The Board's utilization adjustment was prompted by a concern that the methodology which it had previously followed made no adjustment to account for higher load factors due solely to less efficient utilization of aircraft. Until the constraints imposed by the fuel crisis and especially the fuel embargo during the first part of 1974, such an adjustment did not appear necessary. At the time of the Board's most recent evaluation of industry need prior to

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[8] *Id.*

that under review here (October 1974), the base period involved was the year ended June 1974, a period which to some extent reflected the constraints brought about by the fuel crisis but not nearly to the extent that more recent periods have.[9] Since the Board relies upon data for the latest 12 months, each period since the year ended December 1974 is materially affected by the abnormalities stemming from fuel price and availability constraints.

The decision to adjust the utilization rates actually operated in the most recent base period to that achieved in 1972 was not made "arbitrarily" as the petitioners contend, but rather because 1972 represents "the most recent normal calendar-year prior to the development of the fuel crisis in 1973."[10] The adjustment implies only that, over the long run, carrier managements can be assumed to strive for at least the same level of utilization at which they operated prior to the fuel crisis. In our opinion, this is the minimum that should be anticipated.

As for the methodology utilized in making this adjustment, both American and TWA contend that the Board should have compared "ratemaking" utilization rates between the two years as the load-factor adjustment implicitly changes the actual level of utilization achieved. However, in our view, the load-factor adjustment does not affect the utilization rate but, rather, measures the amount of excess capacity in the system in terms of number of aircraft in the carriers' fleets. The production of a given num-

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[9] The trunk carriers' domestic aircraft utilization dropped 11 percent, 8 percent, 7.6 percent, and 1.9 percent from the prior year during the four quarters of 1974. Moreover, it appears that the carriers generally did not include in the "days assigned to service" account of those aircraft which were grounded due to the fuel crisis. If the carriers had done so, their utilization rates would have been significantly lower in the first two quarters of 1974.

[10] Order 75-6-72, p. 4, fn. 3.

ber of available seat-miles (ASM's) is a function of the average number of seats in each aircraft, the total number of aircraft, and the degree to which the aircraft is actually operated. Under the load-factor adjustment, actual ASM's are compared with adjusted, or allowable ASM's,[11] and capacity costs are decreased accordingly. Related investment in flight equipment and interest expense are disallowed, at 75 percent of the percentage difference in actual versus allowable ASM's. The effect of this adjustment is to reflect a reduction in the number of aircraft in the fleet, not a change in the utilization of those aircraft which remain, as the petitioners claim. Accordingly, it is our opinion that a comparison of actual utilization rates for both years is proper.

Therefore, the utilization adjustment does not duplicate, nor double-count, the capacity disallowed under the load-factor adjustment. The adjustment for utilization, with the related reduction in expense for depreciation and insurance and the disallowance of interest and investment, is based upon actual 48-state operating results in keeping with our belief that the abnormal conditions reflected in the year ended March 1975 results should be recognized. Accordingly, the utilization adjustment is made *before* the standard load-factor adjustment. The effect is that the adjustment to a 55 percent load factor is made on the basis of a reduced level of operations and duplication is thereby avoided.

Cost Escalation Factor

Order 75-6-72 explained the computation of the cost escalation factor used by the Board in some detail, and the

[11] The allowable ASM's are those necessary to carry full-fare traffic at a 55 percent load factor.

reasons why its intended purpose "to adjust base-period costs to reflect the level of costs experienced at the effective date of the fare increase" indicated modification in the methodology previously used. The Board explained that using the overall increases in operating expense per available seat-mile (at the standard load factor) from one year to the next accomplishes the desired result as long as unit costs are increasing at a reasonably steady rate. However, this is no longer the situation. As a consequence, a refinement was developed whereby the effect of rising fuel prices on the overall cost increase experienced by the carriers could be estimated separately from that of nonfuel expenses.

It is well known that, while the price of fuel continues to inch upward, the trend has been markedly less precipitous during the first half of this year. It would, therefore, be unrealistic at this time to project last year's trend of escalation into the year ahead. Consistent with this judgment, the Board has estimated the price of fuel at July 1, 1975 at 27.4 cents per gallon. American contends that this estimate is based on incorrect data and that the price of fuel should be higher than the Board's estimate. It is true that, at the time, the Board made its estimate based upon incorrect data.[12] However, data for the month of May (26.9 cents per gallon) indicate almost no increase in fuel prices since April. It would therefore appear that 27.4 cents per gallon is a reasonable estimate of the price the carriers will be paying for fuel as of July 1 and that no change in this respect is warranted.

[12] The price per gallon was originally calculated for the month of April 1975 as 25.93 cents. Upon learning that Eastern's reported fuel data reflected a retroactive adjustment of $4.9 million, the cost per gallon was recomputed as 26.80 cents. CAB Press Release 75-99, June 9, 1975.

The petitioners' major disagreement with the Board's methodology in computing the escalation factor centers upon the assertion that notwithstanding its contention to the contrary, the Board altered its method of computing allowable cost increases for the non-fuel related portion of total costs. We have reviewed our evaluations of the industry's revenue need for the 5 percent increase proposed for December 1973 and the 4 percent increase proposed for November 1974 and are satisfied that our development of a cost escalation factor here has been wholly consistent with earlier methodology except, of course, with respect to isolation of fuel cost.[13]

In its evaluation of both increases the Board based its decision on 12 months ended June results for the respective years. On both occasions the effect of annualizing the inflation factor to the effective date of the tariff equated to the figure calculated from the June data. For example, in Order 73-11-93, the Board calculated the increase in unit cost from the year ended June 30, 1973 over the prior year results as 4.74 percent. Annualizing the average unit-cost increase (4.74 percent) to the end of the base period resulted in a 2.343 percent cost increase.[14] However, the fare increase was to go into effect on December 1 of that same year, and therefore, annualization of the cost increase for an *additional* half year resulted in a total cost increase of

[13] In Order 74-3-96 the Board evaluated the need for a general fare increase of 6 percent. While the Board did make use of the cost escalation factor in its evaluation, the actual value of this factor was of little consequence since the Board was assessing whether there was a need to offset rising fuel prices only, and did not consider a fare increase to offset any increase in non-fuel related expenses.

[14] The 2.343 percent increase is derived from the square root of 1.0474. (The square root is utilized in order to reflect the compounding of increases during the period).

4.74 percent (1.02343 x 1.02343 = 1.0474 cost escalation factor).[15]

In its present evaluation in connection with continuation of the 4 percent increase, the Board has utilized this same technique to approximate the unit cost of non-fuel related expense as of July 1, 1975. However, the resulting cost escalation factor does not equate to the average unit-cost increase for the base period, as was the case above, because it reflects only nine months annualization of costs as compared to a 12-month annualization reflected in the earlier orders. The Board calculated the increase in non-fuel related unit operating costs (at the standard load factor) for the year ended March 31, 1975 as 8.3 percent over the prior year. Annualization of average unit costs during the base period plus the three months from March 31, 1975 to July 1, 1975 results in the 6.1 percent cost escalation factor which we have used.[16]

Belly-cargo Offset

The petitioners' primary objection to annualization of cargo-rate increases is that it constitutes a new adjustment which the Board has not previously made and should not, therefore, be utilized in evaluation of the instant fare in-

[15] Since the tariff went into effect only 5 months after the base period, strict adherence to the methodology would have dictated a reduction in the cost escalation factor to reflect the 5-month period rather than 6-month period. As stated in the order, the Board considered this estimate "quite conservative" and did not therefore make the downward adjustment.

[16] Annualizing the average unit-cost increase for the base period (8.3 percent) to approximate the unit cost *as of* March 31, 1975 equates to 4.1 percent ($\sqrt{1.083}$). To annualize the increase for the additional three months, the increase is equal to 2.0 percent ($\sqrt{1.041}$). Therefore, the total increase over average unit costs for the base period necessary to estimate costs as of July 1 is 6.1 percent (1.041 x 1.020).

creases. As we have previously stated, the present methodology represents a series of refinements as the Board continues to reach a more accurate method of evaluation. The belly-cargo adjustment simply represents a justifiable modification consistent with the reasoning which has heretofore prompted us to annualize passenger-fare increases implemented during the base year, *i.e.*, to reflect and assess the impact of rate increases over an entire twelve-month period.[17]

American contends that the Board failed to adjust cargo traffic "to accurately reflect actual cargo volumes in the forecast year." The only support for this claim is the allegation that domestic cargo revenue ton-miles in scheduled service have declined by 9.5 percent in the first four months of 1975, compared to the same period of 1974. Significantly, the decline in belly-cargo during that period was considerably less, 4.8 percent, and a comparison of the belly-cargo trend during those four months indicates a positive growth rate in the immediate future versus corresponding periods a year ago. Moreover, even adjusting the base-period traffic downward by 4.8 percent, which as indicated does not appear warranted, would have a minimal impact on ROI, and would not have altered our decision.

In summary, we have reexamined the methodology used in analyzing the industry's revenue need for ratemaking purposes against each of the contentions raised by the petitioners. This reexamination has prompted certain limited adjustments as discussed previously, but nonetheless confirms our conclusion that temporary continuation of the

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[17] Eastern points out the Board did not make clear its source for the 8.8 percent increase in belly-cargo yield which it assumed. This estimate was taken from Exhibit 5, p. 1 of 3 of TWA's justification.

4 percent increase is warranted, and that a further increase in fares at this time is not. Most emphatically, we are wholly satisfied that the analytical methodology used in this instance is entirely compatible with the fundamental objectives which the ratemaking standards developed in the *DPFI* are intended to promote.

Accordingly, pursuant to the Federal Aviation Act of 1958, and particularly sections 204, 403, 404, and 1002 thereof,

IT IS ORDERED THAT:

1. Except to the extent granted herein, the petitions for reconsideration filed by American Airlines, Inc., Eastern Air Lines, Inc., and Trans World Airlines, Inc. filed in Docket 27947 are denied;

2. The action on petitions for reconsideration filed by Eastern Air Lines, Inc. and Trans World Airlines, Inc. with respect to Docket 27417 are hereby deferred; and

3. Copies of this order be served upon American Airlines, Inc., Eastern Air Lines, Inc., National Airlines, Inc., Trans World Airlines, Inc., United Air Lines, Inc., the Department of Transportation, and the National Passenger Traffic Association.

This order will be published in the Federal Register.

By the Civil Aeronautics Board:

EDWIN Z. HOLLAND
Secretary

(SEAL)

TIMM, MEMBER, FILED THE ATTACHED CONCURRING STATEMENT.

TIMM, MEMBER, CONCURRING STATEMENT:

At the time that the Board initially decided to disallow these fare increase proposals, I concurred in the ultimate result but expressed concern that several of the new adjustments which the Board then imposed in determining carrier revenue need constituted "novel and unannounced standards upon which the industry and the public have not been given the opportunity for comment." [1] Today the Board once more defends its earlier adoption of such arbitrary policy changes as immediate implementation of a full discount fare adjustment (thereby effectively prejudging the rule-making proceeding by which the Board originally proposed to deal with this issue),[2] and imposition of a novel utilization adjustment for which no advance notice was given.[3]

I discussed some of the most troublesome problems involved in these and other adjustments at some length in my separate statement at that time, and do not intend to belabor these issues by extended repetition now.[4] Suffice

[1] See my concurring statement in Order 75-6-72.

[2] See Order 73-9-108.

[3] In a companion Advance Notice of Proposed Rule-making on Domestic Load Factor Standards, PSDR-43, issued contemporaneously herewith, the Board has once more rejected the institution of a full evidentiary proceeding to determine what the load-factor standard should be for rate-making purposes. In a separate statement attached thereto I pointed out that fairness would require the full airing of issues that only a formal evidentiary proceeding can provide, and I so recommended earlier in my separate statement in Order 75-6-72.

[4] I am pleased that the Board has wisely chosen not to penalize the carriers for offering military discount fares since it has today excluded these fares, for the present at least, from the Phase 5 discount fare adjustment.

it to say that today's Board action perpetuates problems which troubled me then and does not put to rest my doubts about the wisdom or legality of denying the carriers the advance notice which administrative due process would seem to require.

/s/ ROBERT D. TIMM

APPENDIX A

**DOMESTIC TRUNK INDUSTRY
RATE OF RETURN ON INVESTMENT
48-STATE SCHEDULED PASSENGER SERVICE**

**For the Twelve Months Ended
March 31, 1975
(dollar amounts in thousands)**

	Actual	*DPFI Adjustments*[1]	*Other Adjustments*[2]
RPM's (Millions)	105,435	101,094	99,076
ASM's (Millions)	196,893	183,807	180,138
Load Factor	53.5%	55.0%	55.0%
Yield	7.7327¢	7.9897¢	8.2213¢
Passenger Revenue	$8,152,952	$8,077,103	$8,145,291
Operating Revenue	$8,361,926	$8,286,077	$8,354,265
Operating Expense	7,816,941	7,311,470	7,542,615
Operating Profit	$ 544,985	$ 974,607	$ 811,650
Interest	235,951	218,241	196,166
Income Before Tax	$ 309,034	$ 756,366	$ 615,484
Income Tax @ 48%	148,336	363,056	295,432
Net Income	$ 160,698	$ 393,310	$ 320,052
Return Element	$ 396,649	$ 611,551	$ 516,218
Investment	$5,446,233	$5,037,442	$4,595,793
R.O.I.	7.28%	12.14%	11.23%

1 Removal of all discount fares (excluding children's and military); standard seating; and 55 percent standard load factor.

2 Includes Column 2 adjustments plus cost factor, annualization of fare increases, plus adjustments for utilization, grounded aircraft, and belly-cargo.

Note: Column No. 3 includes a reduction of $46 million from Operating Expenses stemming from the traffic costs associated with the annualization of past fare increases at –.7 fare elasticity. Inadvertently, this adjustment was not contained in Attachment E of Order 75-6-72 as it should have been.

Order 75-9-115

**UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.**

**Adopted by the Civil Aeronautics Board
at its office in Washington, D. C.
on the 30th day of September, 1975**

Docket 28363

**Domestic fare increases
proposed by certain carriers**

ORDER OF INVESTIGATION AND SUSPENSION

By tariff revisions[1] marked to become effective October 1, 1975, Eastern Air Lines, Inc. (Eastern) and Continental Air Lines, Inc. (Continental) propose a general domestic fare increase of 3.5 percent; and Trans World Airlines, Inc. (TWA) and Western Air Lines, Inc. (Western) propose a general increase of five percent.[2] With the exception of Western, each also proposes to remove the January 14, 1976 expiration date on the four percent increase first permitted in November 1974 and extended this past June.

1 Revisions to Airline Tariff Publishing Company, Agent, Tariff C.A.B. No. 249.

2 Braniff Airways, Inc. and Frontier Airlines, Inc. had also proposed a 3.5 percent increase for earlier effectiveness. Those proposals were suspended to permit an evaluation of industry revenue need on the basis of June 30, 1975 data (Order 75-9-36). A 4.2 percent fuel surcharge proposed by United Air Lines, Inc. based essentially on a pass-through of anticipated fuel price escalation has also been suspended (Order 75-9-85).

In supporting their proposals, the carriers have followed the methodology used by the Board in assessing fare-increasing proposals before the Board in June 1975, except for modification of the cost-inflation factor and, in the case of TWA, elimination of the utilization adjustment.[3] The carriers allege, *inter alia,* that the Board deviated from its prior technique in calculating the cost-inflation factor and that, based on their recalculation, an increase of 3.5 percent will not raise the ratemaking return on investment (ROI) to the 12 percent standard. TWA alleges that the utilization adjustment was unlawfully adopted and that, in any event, a proper application of such an adjustment would result in no expense disallowance.

Complaints have been filed by the National Passenger Traffic Association (NPTA) and the Council on Wage and Price Stability which, together with answers thereto, are summarized in Attachment A.[4]

Upon consideration of the proposals, the complaints and answers thereto, and all relevant matters, the Board concludes that the proposals to increase present fares by 3.5 or 5.0 percent may be unjust, or unreasonable, or un-

[3] At that time, the Board suspended general increases of five or six percent proposed by certain carriers (Order 75-6-72). The instant proposals were filed prior to the issuance of Order 75-8-99, which denied petitions for reconsideration filed by American Airlines, Inc., Eastern Air Lines, Inc. and Trans World Airlines, Inc.

[4] A joint petition requesting the establishment of emergency procedures in connection with fuel price escalation anticipated due to decontrol of domestic "old" crude has been filed by the Department of Transportation, the Federal Energy Administration, and the Council on Wage and Price Stability. That petition is concerned with possible future developments which cannot be accurately known at this time, and will be dealt with by subsequent order. On the other hand, the Board has recognized the potential consequences of dramatic increases in fuel prices and that special measures may be required to deal with these problems.

justly discriminatory, or unduly prejudicial, or unduly preferential, or otherwise unlawful, and should be investigated. The Board further concludes that such proposals should be suspended pending investigation. However, the Board concludes that NPTA has not set forth sufficient facts to warrant investigation of the proposals to cancel the January 14, 1976 expiration date now applicable to the four percent fare increase first permitted in November 1974, and the request therefor and consequently the request for suspension will be denied and the complaint dismissed.[5]

In each case, the carriers base their proposals on contentions as to the appropriate technique for calculating return on investment which were raised in petitions for reconsideration of Order 75-6-72. These arguments were fully dealt with and disposed of in Order 75-8-99, which denied reconsideration, and need not be further discussed here. TWA (in its current justification) and Eastern (in its answer to NPTA's complaint) accept the Board's methodology with respect to the cost-inflation factor, but argue that their proposals are justified by projecting forward to the new tariff effectiveness date of October 1. While this may be true based on year ended March 1975 data, the Board has consistently used the most recently available experience of the industry and has specifically stated its intention to evaluate new proposals in the context of year ended June 1975 data. On this basis, and applying the same analytical approach used in Order 75-6-72, each of the proposals now before the Board would produce an excessive return on investment by *DPFI* standards (See Attachment B).[6]

[5] Only NPTA complained against extension of the four percent.

[6] The details of the Board's analysis are available for public inspection in the Public Reference Room.

On the other hand, we see no basis for now precluding retention of the four percent increase. An expiration date was first appropriate since the latest data available at that time reflected an abrupt shift in the carriers' traffic mix from discount to full-fare useage which raised a concern that, if traffic volume continued to hold and the change in mix became a longer-term trend, a rollback of the four percent might become warranted. However, not only have neither of these trends progressed, they have, in fact, reversed and have contributed to continuing inadequate industry earnings.

One further matter warrants comment. Our analysis of industry data reveals a particularly troublesome trend of an increasing spread between actual and ratemaking ROI. Excesses in the direction of either total discount-fare traffic or available seats are unmistakably obstacles to the industry's ability to improve its earnings position. Moreover, increases in the proportion of discount-fare traffic must be accompanied by significant increases in load factor in order to maintain a satisfactory revenue/cost relationship. The Board continues to firmly believe that the *DPFI* discount-fare and capacity adjustments are necessary to insure that the normal-fare passenger is not unfairly burdened.

Accordingly, pursuant to the Federal Aviation Act of 1958, and particularly sections 204(a), 403, 404, and 1002 thereof,

IT IS ORDERED THAT:

1. An investigation be instituted to determine whether the fares and provisions described in Attachment C attached hereto, and rules, regulations and practices affecting such fares and provisions, are or will be unjust, unreasonable, unjustly discriminatory, unduly preferential, unduly prejudicial, or otherwise unlawful, and, if found to be

unlawful, to determine and prescribe the lawful fares and provisions, and rules, regulations, or practices affecting such fares and provisions;

2. Pending hearing and decision by the Board, the fares and provisions described in Attachment C hereto are suspended and their use deferred to and including December 29, 1975, unless otherwise ordered by the Board, and that no changes be made therein during the period of suspension except by order or special permission of the Board;

3. The proceeding ordered herein be assigned for hearing before an Administrative Law Judge of the Board at a time and place hereafter to be designated;

4. The proceeding ordered in Docket 28302 be consolidated into this proceeding;

5. Except to the extent granted herein, the complaints in Dockets 28187, 28235 and 28239 are hereby dismissed; and

6. Copies of this order will be filed in the aforesaid tariff and served on Braniff Airways, Inc., Continental Air Lines, Inc., Eastern Air Lines, Inc., Frontier Airlines, Inc., Trans World Airlines, Inc., Western Air Lines, Inc., and the complainants in Dockets 28187, 28235 and 28239 which are hereby made parties to this proceeding.

This order will be published in the Federal Register.

By the Civil Aeronautics Board:

EDWIN Z. HOLLAND
Secretary

(SEAL)

TIMM, MEMBER, FILED THE ATTACHED DISSENTING STATEMENT.

Timm, Member, Dissenting Statement:

By its action today, the Board is once again sacrificing the stability and predictability of the standards adopted in the *Domestic Passenger Fare Investigation* in favor of the perpetuation of such arbitrary policy changes as the immediate implementation of a full discount fare adjustment and the imposition of an aircraft utilization adjustment. These arbitrary determinations which, in view of the economics of the fare proposals presently before the Board, are significantly weighty to justify, in their absence, the implementation of the 3.5 percent increase proposed by Eastern and Continental, have had neither the benefit of public comment nor, in the case of the utilization adjustment, the proper costing technique to include offsetting start-up costs incurred in the reinstatement of unused aircraft. As I have previously noted in my concurring statements to Orders 75-6-72 and 75-8-99, I believe that the principles of the DPFI are being severely jeopardized by the *ad hoc* adoption of these adjustments in the face of the continuing upward trend of aviation costs.

Moreover, of particular concern to me in the present instance, is the majority's failure to include in the cost escalation factor the effects of the recent 10 percent fuel price increase announced by the Organization of Petroleum Exporting Countries (OPEC) for effectiveness October 1, 1975. In Order 75-6-72, the Board devise a refined methodology for developing the cost escalation factor with the intent to have this figure, insofar as it is influenced by fuel prices, more accurately reflect the costs being experienced by the carriers on the proposed effective date of the tariff(s). To disregard these already-announced fuel price increases in the calculation of the cost escalation factor before us both undermines the general principle of the

DPFI that additional costs incurred under operations in line with DPFI standards should be offset by an increase in revenues,[1] and contradicts the Board's intent to use the most recent figures in the determination of fare proposals. This failure is particularly significant in the present circumstances since the fuel costs in the carriers' contracts are geared toward the price paid by the supplier, notwithstanding the delivery date to the carrier. As such, any future fare proposals will be burdened by accumulated costs incurred from the date of the fuel price increase.

In conclusion, I can only reiterate my intention to measure fare proposals by the application of regulatory standards which have been developed in the proper legal forum in a manner consonant with the Board's statutory obligations. Under this standard, I cannot concur with my colleagues' action in suspending the 3.5 percent fare increase proposed by Continental and Eastern, especially in view of the fact that, on competitive grounds, the fare increase would probably not go into effect until, at the earliest, November 1, 1975.

This action by the Board will trigger a new filing almost immediately, for Board methodology and computations indicate a 3 percent increase would be justified at this precise time. Had the Board not inserted the unadjudicated new utilization factor in their June order (see my comments in concurring at that time) the instant fare would be justified in my judgment.

At any rate, the Board has used a razor to slice its way to a decision, when a very sharp knife would have cut through the bureaucratic rate-making tangle that awaits the Board when new cost impact figures become a reality in the next few days.

/s/ Robert D. Timm

[1] *Domestic Passenger Fare Investigation, Phase 7—Fare Levels,* Order 71-4-59/60, April 9, 1971.

ATTACHMENT A

Summary of Complaints and Answers

Complaints

Complaints have been filed by the National Passenger Traffic Association (NPTA) and the Council on Wage and Price Stability (CWPS). The thrust of the NPTA complaint against the increases proposed by Eastern, Braniff, Continental, TWA, and Frontier is that the carriers simply seek further reconsideration of Order 75-6-72, wherein the Board suspended all proposed increases above the present level of fares. NPTA contends that the justifications advanced by the carriers contain little, if any, new or additional data not considered in Order 75-6-72 or subsequently in Order 75-8-99, wherein the Board denied the petitions for reconsideration.

The complaint of CWPS urges the Board to carefully assess the impact which a further fare increase will have on the slowly developing traffic recovery. CWPS expresses its concern that the upward spiral of airline fares, in combination with the recession, has been keeping the discretionary traveler away from air travel; and thus, further fare increases may in fact hurt—not help—the industry's profitability. Finally, CWPS argues that the carriers should be permitted to pass through the higher costs of aviation fuel; that the Board should continue to apply the *DPFI* standards to nonfuel-related fare increases; that pending final decision in the rulemaking proceeding, the Board should adopt a higher ratemaking load factor; and that the Board should reevaluate its measure of fare elasticity.

Answers

Answers have been received from Eastern in response to the complaint by NPTA, and from Continental and TWA in response to the complaint by CWPS.

Eastern states in its answer that nothing advanced by NPTA in its complaint has demonstrated any error in Eastern's approach, and, in fact, it has correctly calculated the inflation factor applicable to the tariff effective date of October 1, 1975. Eastern asserts that there can be no doubt that the deteriorating financial results recently reported by the carriers clearly indicate a need for increased revenues on the part of the industry.

Continental replies to the complaint of CWPS by stating that the effect of the CWPS proposal is to deprive the carriers of sufficient additional revenue to cover the very real cost increases that all carriers are experiencing. Continental states, in addition, that for the purpose of testing the pending fare proposals, the Board is bound to its *DPFI* standards both as a matter of law and fairness, and that they can only be amended by procedures that will afford all parties their due process.

TWA answers the CWPS complaint by stating that air fares have not risen in recent years to exorbitantly high levels; that, in fact, the domestic trunk yield has increased by 28.4 percent, while the general inflation rate has risen by 30.4 percent. TWA asserts that the emergency procedures proposed by CWPS are intended for future increases, whereas the instant proposal deals with already experienced cost increases. TWA contends that the effect of the changes would be to compel the airline industry to absorb even more of its real world cost increases than it must absorb already under existing standards. Finally, TWA states that the suggested modifications to the *DPFI* standards suggested by CWPS are all issues raised previously which the Board dismissed in Order 75-6-72.

ATTACHMENT B

DOMESTIC TRUNK INDUSTRY RATE OF RETURN ON INVESTMENT
48-STATE SCHEDULED PASSENGER SERVICE
for the Twelve Months Ended June 30, 1975
(dollar amounts in thousands)

	Actual (1)	*DPFI Adjustments*[1] (2)	*Other Adjustments*[2] (3)	*Col. 3 Incl. a 3.5% Fare Increase* (4)	*Col. 3 Incl. a 5% Fare Increase* (5)
RPM's (Millions)	104,641	99,041	98,010	95,678	94,719
ASM's (Millions)	199,053	179,942	178,200	173,960	172,217
Load Factor	52.6%	55.0%	55.0%	55.0%	55.0%
Yield (¢)	7.7500	8.0939	8.2162	8.5037	8.6270
Passenger Revenue	$8,109,740	$8,016,250	$8,052,651	$8,136,188	$8,171,385
Operating Revenue	$8,313,066	$8,219,570	$8,255,977	$8,339,514	$8,374,711
Operating Expense	8,014,578	7,165,790	7,629,129	7,447,259	7,372,530
Operating Profit	$ 298,487	$1,053,790	$ 626,847	$ 892,255	$1,002,181
Interest	221,025	184,490	181,992	177,500	175,556
Income Before Tax	$ 77,462	$ 869,297	$ 444,855	$ 714,755	$ 826,625
Income Tax @ 48%	37,182	417,262	213,530	343,082	396,780
Net Income	$ 40,280	$ 452,034	$ 231,325	$ 371,673	$ 429,845
Return Element	$ 261,305	$ 636,524	$ 413,317	$ 549,173	$ 605,401
Investment	$5,459,787	$4,574,890	$4,518,553	$4,409,915	$4,364,010
R.O.I.	4.79%	13.91%	9.15%	12.45%	13.87%

[1] Removal of all discount fares; standard seating; and 55 per cent standard load factor.

[2] Includes Column 2 adjustments plus cost factor, annualization of fare increases, plus adjustments for utilization and belly cargo.

Note: For the purpose of this and future analyses, the Board has refined the methodology to compute the adjustment for belly cargo by offsetting the overall rate of inflation for passenger services of 7.0 percent against the estimated effect of annualizing cargo-rate increases at 6.2 percent.

ATTACHMENT C

TARIFF C.A.B. No. 249
ISSUED BY
AIRLINE TARIFF PUBLISHING COMPANY, AGENT

All increased fares on the following pages:

4th Revised Pages 209 and 210
9th Revised Pages 211 and 212
8th Revised Pages 213 and 214
5th Revised Pages 215 and 216
7th Revised Pages 217 and 218
4th Revised Pages 219, 220 and 221

12th and 13th Revised Page 300
8th Revised Pages 301, 302, 303 and 304
11th Revised Pages 305 and 306
7th Revised Pages 307 and 308
9th Revised Pages 309 and 310
6th Revised Pages 311 and 312
6th and 7th Revised Pages 313 and 314
8th and 9th Revised Pages 315 and 316
5th Revised Pages 317 and 318
7th and 8th Revised Pages 319 and 320
8th Revised Pages 321 and 322
9th and 10th Revised Pages 323 and 324
11th Revised Pages 325 and 326
8th and 9th Revised Pages 327 and 328
9th and 10th Revised Pages 329 and 330
11th Revised Pages 331 and 332
9th Revised Pages 333 and 334
14th Revised Pages 335 and 336
9th Revised Pages 337 and 338

Appendix C

10th Revised Pages 339 and 340
8th Revised Pages 341 and 342
13th and 14th Revised Pages 343 and 344
14th Revised Pages 345 and 346
10th and 11th Revised Pages 347 and 348
9th and 10th Revised Pages 349 and 350
9th Revised Pages 351 and 352
7th Revised Pages 353 and 354
1st Revised Pages 354-A, 254-B, 354-C and 354-D

6th Revised Pages 647 and 648
8th Revised Pages 649 and 650
9th Revised Pages 651 and 652
11th and 12th Revised Pages 653 and 654
6th Revised Pages 655, 656, 657 and 658
10th and 11th Revised Pages 659 and 660
6th Revised Pages 661 and 662
10th Revised Pages 663 and 664
9th Revised Pages 665, 666, 667 and 668
8th Revised Pages 669, 670, 671 and 672
8th and 9th Revised Pages 673 and 674
4th Revised Pages 674-A and 674-B
1st Revised Pages 674-C and 674-D

6th Revised Page 749
7th Revised Page 749 (except between Anchorage on the one hand and Portland, Oregon and Seattle on the other)
6th Revised Pages 750, 751 and 752
10th Revised Pages 753 and 754
4th Revised Pages 755 and 756
5th Revised Page 756 (except between Kodiak on the one hand and Portland, Oregon and Seattle on the other)
17th Revised Pages 757 and 758

Appendix C

8th Revised Pages 759 and 760
7th Revised Pages 761 and 762
6th Revised Pages 763

All fares on the following pages which are reissues of fares suspended herein on the above pages:

14th Revised Page 300
9th Revised Pages 301 and 302
10th Revised Pages 315 and 316
11th and 12th Revised Pages 323 and 324
10th Revised Pages 327, 328, 333 and 334
9th Revised Pages 341 and 342
15th Revised Pages 343 and 344
11th and 12th Revised Pages 349 and 350

13th Revised Pages 653 and 654
7th Revised Pages 655 and 656
10th Revised Pages 665 and 666
9th Revised Pages 669, 670, 671 and 672

7th Revised Page 750
5th Revised Page 755
18th and 19th Revised Pages 757 and 758
9th Revised Pages 759 and 760
8th Revised Pages 761 and 762